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IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

No. 79-927

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Petitioner,

v.

INVESTMENT COMPANY INSTITUTE,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF *AMICUS CURIAE* SECURITIES INDUSTRY ASSOCIATION IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

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The Securities Industry Association, with the consent of the parties, submits this brief *amicus curiae* in opposition to the petition for a writ of certiorari.

INTEREST OF THE AMICUS

The Securities Industry Association ("SIA") is a national trade association representing approximately

500 organizations responsible for over 90 percent of the securities brokerage and investment banking business of the nation. Its membership is a cross-section of the diverse facets of the securities business and encompasses members of the national securities exchanges as well as firms which are not members of such exchanges. The business of its members includes retail and institutional brokerage, over-the-counter market-making, underwriting and other investment banking activities. Many SIA members sponsor open- and closed-end investment companies, which permit the investing public to pool investment capital and obtain the advantages of a broader portfolio of investments than otherwise would be available to most individual investors. The SIA and its members have a clear interest in the subject matter of this proceeding, which is whether the banking industry should be permitted to expand into the securities business by sponsoring closed-end investment companies.

REASONS FOR DENYING THE WRIT

1. *The narrow legal issue decided below, namely, that bank holding companies should not organize, sponsor and control closed-end investment companies, has little impact on current activities of bank holding companies.*

Between 1972, when Regulation Y of the Board challenged herein first became effective, and 1977, when the Investment Company Institute filed its petition for reconsideration with the Board, apparently only four out of the over 2,200 registered bank holding companies undertook to sponsor closed-end investment companies. Moreover, based on the statistics in the Petition for Certiorari, the total net assets of the ten closed-end investment companies presently man-

aged by any kind of banking organization amount to approximately only one percent of the total assets of the registered investment companies in the United States.[1] Thus, the immediate impact of the narrow holding below is slight. In an attempt to breathe significance into the decision in terms of present day banking practices, Petitioner and the other *Amici* address an issue that was neither raised nor decided below, namely, whether bank holding companies can provide investment advisory services to investment companies. As stated by the Court of Appeals below:

> . . . we do not reach, and are not to be taken as expressing any view on, the question of whether bank holding companies and their non-bank subsidiaries may, either under the present regulation or one more narrowly drawn, render solely investment advice to closed-end investment companies, as distinct from sponsoring, organizing, managing, or controlling such companies.[2]

2. *This Court already has addressed the controlling Congressional policy involved: that the commercial banking industry should not be permitted to sponsor or operate investment funds marketed to the general public.*

Investment Company Institute v. *Camp*[3] struck down an attempt by the Comptroller of the Currency to permit national banks to operate open-end investment funds. In holding such activity violated Sections 16 and 21 of the Glass-Steagall Act,[4] this Court de-

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[1] *See* Petition for Writ of Certiorari ("Pet.") at 11 and *SEC Final Report on Bank Securities Activities* at 148 (1977).

[2] Pet., App. A at 48a-49a.

[3] 401 U.S. 617 (1971).

[4] 12 U.S.C. §§ 24 (Seventh) and 378.

scribed the concerns which led Congress to insist that commercial banking be divorced completely from investment banking. Among the principal concerns were (A) impairment of public confidence in the bank if the securities affiliate fares badly since the bank and the affiliate become closely associated in the public mind; (B) pressure on the bank to make its credit facilities and possibly even unsound loans more readily available to companies in whose securities the affiliate has invested or otherwise become involved; (C) possible risk that bank depositors would suffer losses on the investments they purchased in reliance on the relationship between the bank and its securities affiliate; (D) danger that the bank would be tempted to make customer loans more liberally for purposes of facilitating the purchase of its affiliates' securities; and (E) conflict between the promotional interest of the investment banker and the obligation of the commercial banker to render disinterested investment advice.[5]

> In sum, Congress acted to keep commercial banks out of the investment banking business largely because it believed that the promotional incentives of investment banking and the investment banker's pecuniary stake in the success of particular investment opportunities was destructive of prudent and disinterested commercial banking and of public confidence in the commercial banking system.[6]

While in *Camp* the bank operated the fund itself, the concerns expressed above apply with equal force to sponsorship of investment funds by a bank holding company. Thus, the Board properly concluded in Reg-

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[5] 401 U.S. at 629-633.

[6] *Id.* at 634.

ulation Y that the Glass-Steagall Act, as interpreted in *Camp,* prohibits a bank holding company from sponsoring an open-end investment company.[7] The Board went on, however, in that portion of Regulation Y challenged below, to draw a distinction between open- and closed-end funds that has no substance in terms of the concerns of Congress set forth above.

Although open- and closed-end investment companies differ in certain aspects of their operations, both are formed for the purpose of "buying and selling securities acquired purely for investment or speculative purposes."[8] In both cases, the bank holding company "would necessarily put its reputation and facilities squarely behind that fund and the investment opportunity that fund offered" and poor performance of the fund "could bring about a perhaps unjustified loss of public confidence" in its affiliated bank.[9] The fact that a closed-end fund does not stand ready to redeem its shares and typically sells its stock to the public less frequently than an open-end fund does not materially reduce the financial risks inherent in the fund's operation or the loss of public confidence that would attend its failure. Moreover, the other concerns underlying the Glass-Steagall Act that are reiterated above from *Camp* regarding banking industry sponsorship of investment funds apply with equal force to closed-end and to open-end funds. Lastly, as the Court below found, bank holding company sponsorship and control of closed-end funds poses the risk of centralization of economic power regarding which, the Court of Appeals

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[7] *See* 12 C.F.R. § 225.125(f) [Pet., App. F at 85a].

[8] 401 U.S. at 635.

[9] *Id.* at 637.

noted, Congress was particularly concerned when it enacted the 1970 Amendments to the Bank Holding Company Act.[10] It is simply not realistic, therefore, to assume, as the Board does, that Congress intended emphatically to prohibit bank holding companies from sponsoring one kind of investment fund but not the other. At the very least, such a dubious distinction should not be drawn without a much clearer and more specific expression of Congressional intent than that relied upon by the Board.

3. *The issue presented is one of several issues involving securities and other non-banking activities of bank holding companies that are currently under active consideration by Congress.*

The Subcommittee on Financial Institutions Supervision, Regulation and Insurance of the House Committee on Banking, Finance and Urban Affairs recently conducted extensive hearings on three bills, H.R. 1539 (which would permit banks to underwrite and deal in revenue bonds) and H.R. 2747 and H.R. 2856 (which would limit substantially the non-banking activities of bank holding companies). H.R. 2747, styled the "Bank Holding Company Amendments of 1979," in addition to codifying the decision of this Court in *Camp* and that of the Court of Appeals below regarding sponsorship of publicly marketed investment funds, would also preclude a bank holding company from being affiliated with any firm that acts as an investment adviser to such funds. H.R. 2856 would restrict more severely the activities in which bank holding companies may engage to those which are a

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[10] Pet., App. A at 46a.

"proper and necessary incident" to the business of banking.[11]

During the hearings, the Chairman of the Securities and Exchange Commission noted, *inter alia,* that the whole structure of the securities industry was undergoing very substantial change since elimination in 1975 of fixed brokerage commissions and the effort to develop a national market system.[12] He also observed that banks may achieve competitive advantages over securities firms because there are significant differences in the laws and regulations governing them from those governing securities firms.[13] The Chairman concluded:

> The Commission shares the concerns addressed in H.R. 2747 and H.R. 2856 with respect to the proper role of banks in securities activities. . . . [T]he bills now before you raise important questions with respect to the health of our capital markets, and the continued validity of the traditional distinction between commercial and investment banking. We favor competition. Indeed, we are charged by our statutes to promote it. But these bills raise questions about the dangers of excessive concentration of economic power, about the financial service needs of the public and private sectors, about potential conflicts of interest

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[11] A similar bill currently pending in the Senate, S. 39, would impose comparable and equally strict limitations on bank holding companies.

[12] Statement of Harold M. Williams, Chairman of the Securities and Exchange Commission, before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance of the House Committee on Banking, Finance and Urban Affairs, regarding H.R. 1539, H.R. 2747 and H.R. 2856, 96th Cong., 1st Sess., Oct. 17, 1979, at 5.

[13] *Id.* at 14-17.

> and about unequal regulation. These are important, broad and complex issues which need to be addressed by the Congress.[14]

Acceptance of the Board's tenuous reading of its authority under the Bank Holding Company Act would give it a charter to depart substantially from the clear policy expressed by Congress and thereby alter the existing delicate competitive balance between the banking and securities industries at a time when Congress is actively reexamining the broader issues raised by the banking industry's multipronged efforts to reenter the securities business. Because of the many complex and interrelated factors to be weighed, it would be more appropriate for Congress, rather than the Board, to provide the necessary policy guidance in this area, as that body has in the past.

4. *The decision below is clearly correct.*

Section 4(c)(8) of the Bank Holding Company Act is a narrowly drawn exception to the general thrust of that Act, which is to *restrict* the non-banking activities of bank holding companies. The Board is authorized to permit bank holding companies to engage only in those activities it finds "to be so closely related to banking . . . as to be a proper incident thereto." [15] Moreover, as Judge McGowan, speaking for a unanimous panel, carefully traced, the legislative history of the Bank Holding Company Act shows that it was "a loophole-closing law designed to further the Glass-Steagall Act's overarching policy . . . of divorcing investment from commercial banking." [16]

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[14] *Id.* at 13, 17-18.

[15] 12 U.S.C. § 1843(c)(8) [Pet., App. G at 91a].

[16] Pet., App. A at 30a.

The Board's expansive reading of Section 4(c)(8) as authorizing it to permit bank holding companies to organize, sponsor and control closed-end investment companies is totally at odds with this purpose of the Bank Holding Company Act. It is equally at odds with the plain meaning of the language of Section 4(c)(8), which cannot reasonably be read as suggesting that securities activities expressly forbidden to banks can nevertheless "be so closely related to banking . . . as to be a proper incident thereto."

In the final analysis, the opinion properly concludes, as this Court recognized in *Camp,* that Congress did not want the banking industry involved in sponsoring investment funds marketed to the public. This left the Court of Appeals with no reasonable basis on which to uphold the Board's action to the contrary.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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